

**ACC501**  
**7 Final-Term Paper Solved**  
**By**  
**مونا محمد ناسر سادیق**

FINALTERM EXAMINATION  
Fall 2008  
ACC501- Business Finance (Session - 1)  
Marks: 81

Question No: 1 ( Marks: 1 ) - Please choose one  
Which of the following is the difference between current assets and current liabilities?

Surplus Asset  
Short-term Ratio  
**Working Capital**  
Current Ratio

Question No: 2 ( Marks: 1 ) - Please choose one  
Which of the following statement is considered as the summary of the effect of revenues and expenses over a period of time?

**Income Statement**  
Balance Sheet  
Cash Flow Statement  
Retained Earning Statement

Question No: 3 ( Marks: 1 ) - Please choose one  
If sales revenue was Rs. 100,000 , accounts receivable decreased by R s. 4,000, and inventory increased by Rs. 3,000, cash received from customers would be:

Rs. 107,000  
Rs. 104,000  
**Rs. 101,000**  
Rs. 93,000

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**100,000 + 4000(inflow) – 3000(outflow)**

•We had sales of \$500, while accounts receivable rose by \$30 over the year, so cash inflow is \$500 – 30 = \$470

Question No: 4 ( Marks: 1 ) - Please choose one

Which of the following statement is the best representative of vertical analysis?

Vertical analysis in the income statement causes all accounts to be related as a percentage of net income.

**Vertical analysis in the balance sheet causes all accounts to be related as a percentage of total assets.**

Percentages used in vertical analysis make identifying trends difficult.

Percentages can be used in the balance sheet without being associated with the numbers they represent.

<http://answers.yahoo.com/question/index?qid=20100804021544AABSZrZ>

Question No: 5 ( Marks: 1 ) - Please choose one

Kamran just won a lottery and want to put some money away so that he will have Rs. 75,000 for his Childs school education 18 years from now. He can earn 7.5 percent compounded annually. How much does he need to invest today?

Rs. 15,763

Rs. 17,271

Rs. 18,980

**Rs. 20,404**

**Use Present Value formula =  $PV = FV / (1+r)^t$**

Question No: 6 ( Marks: 1 ) - Please choose one

You need Rs. 2,000 to buy a new DVD player for your car. If you have Rs. 800 to invest at 5 percent compounded annually, how long will you have to wait to buy the DVD player?

8.42 years

14.58 years

15.75 years

**18.78 years p59**

**Number of periods =  $\frac{\text{natural log} [(FV * i) / (PV * i)]}{\text{natural log} (1 + i)}$**

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Question No: 7 ( Marks: 1 ) - Please choose one

How much must be deposited at 15% each of the next 7 years to have Rs. 4,565?

Rs. 452.75

Rs. 570.50

Rs. 350.20

**Rs. 412.50**

$$4565 = C * [(1+0.15)^7 - 1]/0.15$$

Solve for C

Question No: 8 ( Marks: 1 ) - Please choose one

What amount a borrower would pay at the end of second year with a 4 -year, 12%, interest- only loan of Rs. 3,000?

Rs. 360

Rs. 2,000

Rs. 3,000

**Rs. 3,360** p69

**Interest-Only Loans**

•Calls for the borrower to pay interest each period and to repay the entire principal at some time in the future.

•With a 3-year, 10%, interest-only loan of \$1,000, the borrower would pay  $\$1,000 \times 0.10 = \$100$  in interest at the end of first and second years,

•At the end of third year, he would return \$1000 plus the \$100 in interest for that year.

Question No: 9 ( Marks: 1 ) - Please choose one

Which of the following is the expected rate of return on a bond if bought at its current market price and held to maturity?

Current Yield

**Yield To Maturity**

Coupon Yield

Capital Gains Yield

Question No: 10 ( Marks: 1 ) - Please choose one

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The price of a Rs.1,000 -face value bond is Rs.1,000. What will be the yield to maturity if there is a coupon payment of Rs. 80 for 6 years?

**Greater than 8% p77**

Lower than 8%

Equal to 8%

Cannot be determined without more information

**Bond value =  $C \times [1 - 1 / (1 + r)^t] / r + F / (1 + r)^t$**

Where: C = the promised coupon payment

F = the promised face value

t = number of periods until the bond matures

r = the market's required return, YTM

Question No: 11 ( Marks: 1 ) - Please choose one

Which of the following short-term rating by PACRA denotes an inadequate capacity to ensure timely repayment?

A

B

**C**

D

Question No: 12 ( Marks: 1 ) - Please choose one

Which one of the following statements is INCORRECT regarding zero coupon bonds?

Zero coupon bonds pay no interest at all.

Zero coupon bonds are offered at a price that is much lower than its stated value.

**The issuer of a zero coupon bond deducts interest every year because interest is actually paid every year.**

The issuer of a zero coupon bond deducts interest every year even though interest is not actually paid every year.

Question No: 13 ( Marks: 1 ) - Please choose one

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An investment should be accepted if the net present value is \_\_\_\_\_ and rejected if it is \_\_\_\_\_.

Positive; positive  
**Positive; negative p105**  
Negative; negative  
Negative; positive

Question No: 14 ( Marks: 1 ) - Please choose one  
An investment is acceptable if its calculated payback period is \_\_\_\_\_ than/to some specified number of years.

More  
**Less p105**  
Equal  
None of the given options

**“An investment is acceptable if its calculated payback period is less than some specified number of years.”**

Question No: 15 ( Marks: 1 ) - Please choose one

The rate at which NPV equals to zero is called :

Average Accounting Return (AAR)  
**Internal Rate of Return (IRR)**  
Required Rate of Return (RRR)  
Weighted Average Cost of Capital (WACC)

Question No: 16 ( Marks: 1 ) - Please choose one

A project whose acceptance prevents the acceptance of one or more alternative projects is referred to as:

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- A mutually exclusive project  
An independent project  
**A dependent project**  
A contingent project

[http://wps.pearsoned.co.uk/ema\\_uk\\_he\\_wachowicz\\_fundfinman\\_12/26/6680/1710103.cw/content/index.html](http://wps.pearsoned.co.uk/ema_uk_he_wachowicz_fundfinman_12/26/6680/1710103.cw/content/index.html)  
Q#20

Question No: 17 ( Marks: 1 ) - Please choose one

\_\_\_\_\_ Cost is an outlay that has already occurred and hence is not affected by the decision under consideration.

**Sunk**

- Opportunity  
Fixed  
Variable

Question No: 18 ( Marks: 1 ) - Please choose one

\_\_\_\_\_ Cost refers to the cash flows that could be generated from an asset the firm already owns provided it is not used for the project in question.

**Sunk**

- Opportunity  
Fixed  
Variable

Question No: 19 ( Marks: 1 ) - Please choose one

If two projects are \_\_\_\_\_, the fact that they have unequal lives will not affect the analysis.

- Mutually exclusive

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Dependent

**Independent**

Correlated

<http://www.docstoc.com/docs/8183229/CFA-Quiz-11>

Question ID: 17328

Which of the following statements is **FALSE**?

- A. An incremental cash flow represents the change in the firm's total cash flow that occurs as a direct result of taking a project.
- B. If two projects are independent, the fact that they have unequal lives does not affect the analysis.
- C. A sunk cost is one that has already occurred.
- D. Financing charges are considered as in the incremental cash flow analysis.

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Explanation: Correct answer: D

Question No: 20 ( Marks: 1 ) - Please choose one

Mr. A, as a financial consultant, has prepared a feasibility report of a project for XYZ Company that the company is planning to undertake. He has suggested that the project is feasible. The consultancy fee paid to Mr. A will be considered as:

**Sunk cost p120**

Opportunity cost

Both sunk cost and opportunity cost

Neither sunk cost nor opportunity cost

**Sunk Costs**

- A cost that has already been incurred and cannot be recouped and therefore should not be considered in an investment decision
- e.g. a consultant's fee for evaluating the option of launching a new product

Question No: 21 ( Marks: 1 ) - Please choose one

Which one of the following is TRUE about the difference between debt and common stock?

Debt is ownership but equity is not

Creditors have voting power while stockholders do not

**Interest payments are promised while dividend payments are not**

Both stockholders and bondholders have voting privileges

[http://highered.mcgraw-hill.com/sites/0073405132/student\\_view0/chapter7/chapter\\_quiz.html](http://highered.mcgraw-hill.com/sites/0073405132/student_view0/chapter7/chapter_quiz.html) Q#9

Question No: 22 ( Marks: 1 ) - Please choose one

Which one of the following typically applies to preferred stock but not to common stock?

Dividend yield

**Cumulative dividends**

Voting rights

Tax deductible dividends

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Which of the following model is considered as the best approach to explicitly establish an optimal inventory level ?

- Dividend growth model
- Capital asset pricing model
- Economic order quantity model p190**
- None of the given options

Question No: 28 ( Marks: 1 ) - Please choose one  
Unsystematic Risk is also known as :

- Diversifiable Risk p142**
- Market Risk
- Non-diversifiable Risk
- None of the given options

Question No: 29 ( Marks: 1 ) - Please choose one  
Which of the following is an example of unsystematic risk ?

- Increasing Recession
- Rise in Interest Rate
- Rise in Inflation
- Strike call in a company**

Question No: 30 ( Marks: 1 ) - Please choose one  
Total portfolio risk is equal to :

- Systematic risk plus diversifiable risk p141**
- Unsystematic risk plus non-diversifiable risk
- Market risk plus unsystematic risk
- All of the given options

Question No: 31 ( Marks: 1 ) - Please choose one  
Which of the following type of risk is essentially eliminated by diversification ?

- Systematic Risk
- Market Risk
- Unsystematic Risk p141**
- None of the given options

**“Unsystematic risk is essentially eliminated by diversification, so a relatively large portfolio has almost no unsystematic risk.”**

Question No: 32 ( Marks: 1 ) - Please choose on

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What will be the risk premium for a stock that has an expected return rate of 15% and a risk-free rate of 9% ?

**6 %** p136

9 %

15 %

24 %

**Risk Premium**

•The difference between the return on a risky investment and that on a risk-free investment.

•Risk Premium = expected return – Risk-free rate  
=  $E(R_u) - R_f$

Question No: 33 ( Marks: 1 ) - Please choose one

Which of the following is referred as a statistical measure of the variability of a distribution around its mean ?

Probability distribution

The expected return

**The standard deviation**

Coefficient of variation

<http://wps.pearsoned.co.uk/wps/grader> Q#3

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Question No: 34 ( Marks: 1 ) - Please choose one  
The MC Inc. purchased a share of common stock exactly one year ago for Rs. 45. During the past year the common stock paid an annual dividend of Rs. 2.40. The firm sold the stock today for Rs. 80. What is the rate of return the firm has earned?

- 5.3%
- 194.2%
- 83.11%**
- 94.2%

**The correct answer: 83.11%.**

**Return is over the two-year period and includes both dividends and capital gains. Return = [(\$2.40) + (\$80 - \$45)] / \$45 = 83.11%**

You pay 45  
you sell it for 80  
you made 2.40 in dividends

Always remember the simple rate of return formula as New - Old / Old  
New is the amount you made for holding the stock, 80 + 2.40.  
Old is what you paid for it =45  
 $82.40 - 45 / 45 = 83.11\%$

Question No: 35 ( Marks: 1 ) - Please choose one

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The total market value of a companies stocks is calculated as Rs. 250 million and the total market value of the company s debt are calculated as Rs.150 million .What percent of the firms financing is debt ?

**37.50%**

50.00%

62.50%

70.00%

**250+150=400**

**250/400=0.625**

**0.625\*100=62.5 is equity and**

**100-62.5=37.5 is debt**

Question No: 36 ( Marks: 1 ) - Please choose one

If the book value exceeds the market value, then the difference is treated as a \_\_\_\_\_ for tax purposes.

Profit

**Loss**

Surplus

None of the given options

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Question No: 37 ( Marks: 1 ) - Please choose one  
Market value exceeds book value by Rs.150,000. What will be the after-tax proceeds if there is a tax rate of 35 percent ?

**Rs. 97,500** p129

Rs. 105,600

Rs. 115,000

Rs. 150,000

• This \$160,000 excess of market value over book value is taxable. So after tax proceeds will be  
 $150000 * (1 - 35)\% = 97500$

Question No: 38 ( Marks: 1 ) - Please choose one  
The cost of common equity for a firm is:

**The required rate of return on the company's stock**

The yield to maturity on the bond

The risk-free rate

The market risk premium

<http://highered.mcgraw-hill.com/novella/QuizProcessingServlet> Q#7

Question No: 39 ( Marks: 1 ) - Please choose one

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The book value of a system is Rs. 30,220 at the end of year 4 of its life. What will be the total after-tax cash flow from sale if we sell this system for Rs. 15,000 at this time? (Tax rate is 35%)

Rs. 15,000

Rs. 15,220

**Rs. 20,327 p128**

Rs. 45,220

•The book value at the end of year 4 is \$27,648. if we sell the system for \$10,000 at that time, we will have a loss of \$17,648 for tax purposes.

•We get \$10,000 from buyer

•We save  $0.34 \times \$17,648 = \$6,000$  in taxes. So the total after tax cash flow from the sale is a \$16,000 cash inflow

$$30220 - 15000 = 15220 * 35\% = 5327 + 15000 = 20327$$

Question No: 40 ( Marks: 1 ) - Please choose one

Four years ago, Mr. Ajmal purchased a car for Rs. 300,000. Now he wants to sell his car . Based on historical averages, his car worth 25% of the purchase price and he sells his car at this price. What would be his tax liability if the depreciation schedule shows a book value of Rs. 27,250 for the car ? (Tax rate is 35%)

Rs. 14,875.75

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**Rs. 16,712.50**

Rs. 25,000.00

Rs. 62,500.25

$300000 * 25\% = 75000$

$75000 - 27250 = 47750 * 35\% = 16712.50$

Question No: 41 ( Marks: 1 ) - Please choose one  
Miss Nadia purchased a car for Rs. 500,000. Based on historical averages, this car is worth 30% of the purchase price now and it is being sold at this price. What is the cars market value ?

Rs. 51,875

Rs. 112,500

**Rs. 150,000**

Rs. 350,000

$(500000 * 30\%)$

Question No: 42 ( Marks: 1 ) - Please choose one  
Leverage is considered beneficial when company s EBIT is relatively

\_\_\_\_\_.

**High p151**

Low

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Zero  
None of the given options

Question No: 43 ( Marks: 3 )  
Write down the property classes for MACRS method of depreciation.

Question No: 44 ( Marks: 3 )  
Write down the primary shortcomings of payback period rule.

Question No: 45 ( Marks: 3 )  
Define EDI (Electronic Data Interchange) and write down its advantages briefly.

Question No: 46 ( Marks: 5 )  
What is the difference between temporary current assets and permanent current assets?

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Question No: 47 ( Marks: 5 )

If you have a portfolio that is worth Rs. 200,000 consisting of three stocks A, B, C and D. Assume you have divided your investment equally in these four stocks. Expected returns on Stocks A, B, C and D are 20%, 25%, 15% and 12% respectively. Calculate the portfolio expected return.

Question No: 48 ( Marks: 10 )

SNT & Co. has the following Target capital structure:

Debentures = Rs. 5.00 Billion  
Preferred shares = Rs. 2.65 Billion  
Common shares = Rs. 9.35 Billion

Total = Rs. 17 Billion

Bonds carry an interest rate of 11.5%. Common stocks and Preferred stocks have a return of 15.50 % and 12% respectively and corporate tax rate is 40%. Compute the present Weighted Average Cost of Capital (WACC) for SNT & Co.

Question No: 49 ( Marks: 10 )

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Standard Manufacturing Company (SMC) needs one of two machines. Machine X costs Rs. 25,000 and has cash flows of Rs. 8,000 a year for six years. Machine Y costs Rs. 30,000 and has cash flows Rs. 7,000 a year for six years. SMC has 12% cost of capital. Calculate each machine Payback Period and NPV (Net Present Value) and evaluate the results.

**FINAL TERM EXAMINATION**  
**Spring 2009**  
**ACC501- Business Finance**

**Question No: 1 ( Marks: 1 ) - Please choose one**

**Which of the following refers to a conflict of interest between principal and agent?**

- Management Conflict
- Interest Conflict
- **Agency Problem**
- None of the given options

**Question No: 2 ( Marks: 1 ) - Please choose one**

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Which of the following term refers to the ease and quickness with which assets can be converted to cash?

- Analysis
- Structuring
- Budgeting
- **Liquidity**

Question No: 3 ( Marks: 1 ) - Please choose one  
Product costs do NOT include which of the following?

- Raw material
- Direct labor
- Manufacturing overhead
- **Administrative expenses**

<http://www.learnmanagerialaccounting.com/FreeMaterial/productperiod/index.html>

**Product Costs: Include all costs that are required to make a product**  
**Product costs are: Direct Material, Direct Labor, Manufacturing Overhead**

Are included as part of inventory and shown on the balance sheet until the product is sold. Product costs are often called “inventoriable costs” or “manufacturing costs”.

When the product is sold, the costs are “matched” to the sales revenue and reported on the income statement as cost of goods sold

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**Question No: 4 ( Marks: 1 ) - Please choose one**

**Which of the following can be computed by using the information only from balance sheet?**

- **Equity multiplier p38**
- Inventory turnover
- Receivable turnover
- Return on equity

• **Equity Multiplier = Total Assets / Total Equity**

**Question No: 5 ( Marks: 1 ) - Please choose one**

**Which of the following is CORRECT regarding the present value discount factor?**

- It is always greater than 1.0
- **It decreases as the discount rate increases**
- It is equal to zero when discount rate is zero
- It increases as the time period increases

<http://answers.yahoo.com/question/index?qid=20100804022124AAsWb55>

Question No 1:

Which of the following is CORRECT regarding the present value discount factor?

It decreases as the discount rate increases

Source(s):

35 years of accounting experience

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**Question No: 6 ( Marks: 1 ) - Please choose one**

**How much must be deposited at 8% each of the next 20 years to have Rs. 10,296.44?**

- **Rs. 225**
- Rs. 341
- Rs. 410
- Rs. 452

$$FV = c * [(1+i)^n - 1] / i$$

**Question No: 7 ( Marks: 1 ) - Please choose one**

**In order to compare different investment opportunities (each with the same risk) with interest rates reported in different manners you should:**

- **Convert each interest rate to an effective annual rate**
- Convert each interest rate to a monthly nominal rate
- Convert each interest rate to an annual nominal rate
- Compare the published annual rates

[http://highered.mcgraw-hill.com/sites/0072946733/student\\_view0/chapter5/multiple\\_choice\\_quiz.html](http://highered.mcgraw-hill.com/sites/0072946733/student_view0/chapter5/multiple_choice_quiz.html)

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**Question No: 8 ( Marks: 1 ) - Please choose one**

**You have Rs. 1,000 to invest. You have 2 choices; first is the savings account A, which earns 8.75 percent compounded annually and second is the savings account B, which earns 8.50 percent compounded monthly. Which account should you choose and why?**

- Account A; because it has a higher effective annual rate
- **Account B; because it has a higher effective annual rate**
- Account A; because it has the higher quoted rate
- Account B; because the quoted rate is higher

**EAR (A) = 8.75**

**EAR (B) = 9.10**

**P 68**

- EAR is computed in three steps
- Divide the quoted rate by the number of times the interest is compounded
- Add 1 and raise it to the power of number of times the interest is compounded.
- Subtract 1

So

$$\text{EAR} = (1 + \text{Quoted rate} / m)^m - 1$$

*Where m is the number of times the interest is compounded*

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**Question No: 9 ( Marks: 1 ) - Please choose one**

**What will be the value of a Rs. 1,000 face-value bond with an 8% coupon rate at 8% required rate of return?**

- **More than its face value**
- Less than its face value
- Equal to its face value
- Cannot be determined without more information

**Question No: 10 ( Marks: 1 ) - Please choose one**

**Which of the following statement is FALSE regarding debt?**

- Debt is not an ownership interest in the firm.
- Unpaid debt can result in bankruptcy or financial failure.
- **Debt provides the voting rights to the bondholders. P77&78**
- Corporation s payment of interest on debt is fully tax deductible.

**Question No: 11 ( Marks: 1 ) - Please choose one**

**The relationship between real and nominal returns is described by the:**

- M&M Proposition
- Capital Asset Pricing Model
- **Fisher s Effect**
- BCG Matrix

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**Question No: 12 ( Marks: 1 ) - Please choose one**  
Investors demand a higher yield as compensation to the risk of possible default.  
This extra premium is called:

- **Default risk premium p90**
- Taxability premium
- Interest rate risk premium
- Inflation risk premium

**Question No: 13 ( Marks: 1 ) - Please choose one**  
For which type of stocks, the dividends grow at a constant rate?

- Zero Growth Stocks
- **Constant Growth Stocks p92**
- Non-Constant Growth Stocks
- None of the given options

**Question No: 14 ( Marks: 1 ) - Please choose one**  
In which type of voting, each shareholder is entitled one vote per share times the number of directors to be elected?

- Straight Voting
- Statutory Voting
- **Cumulative Voting**
- None of the given options

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**Definition of 'Cumulative Voting'**

The procedure of voting for a company's directors; each shareholder is entitled one vote per share times the number of directors to be elected.

This is sometimes known as 'proportional voting'.

Read

more: <http://www.investopedia.com/terms/c/cumulativevoting.asp#ixzz202OUp5WY>

**Question No: 15 ( Marks: 1 ) - Please choose one**

**In which of the following procedure of voting for a company's directors, each shareholder is entitled to one vote per share ?**

- Straight Voting
- Proportional Voting
- **Cumulative Voting**
- None of the given options

**Definition of 'Cumulative Voting'**

The procedure of voting for a company's directors; each shareholder is entitled one vote per share times the number of directors to be elected.

This is sometimes known as 'proportional voting'.

Read

more: <http://www.investopedia.com/terms/c/cumulativevoting.asp#ixzz202PsQWC2>

**Question No: 16 ( Marks: 1 ) - Please choose one**

**Which of the following is the price that the dealer wishes to pay for a share ?**

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- Simple Price
- **Bid Price p100**
- Strike Price
- Complex Price

• The price that the dealer wishes to pay is the **bid price** and the price at which the dealer sells the securities is called the strike price.

**Question No: 17 ( Marks: 1 ) - Please choose one**

Suppose the initial investment for a project is Rs. 160,000 and the cash flows are Rs. 40,000 in the first year and Rs. 90,000 in the second and Rs. 50,000 in the third. The project will have a payback period of:

- **2.6 Years**
- 3.1 Years
- 3.6 Years
- 4.1 Years

Payback Period = Years before recovery + (Uncovered Cost / Cash Flow from which the cost is to be covered)

**Question No: 18 ( Marks: 1 ) - Please choose one**

The XYZ Corporation is considering an investment that will cost Rs. 80,000 and have a useful life of 4 years. During the first 2 years, the net incremental after-tax cash flows are Rs. 25,000 per year and for the last two years they are Rs. 20,000 per year. What is the payback period for this investment ?

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- 3.2 Years
- **3.5 Years**
- 4.0 Years
- Cannot be determined from the given information

**Question No: 19 ( Marks: 1 ) - Please choose one**

**Which of the following measures the present value of an investment per dollar invested ?**

- Net Present Value (NPV)
- Average Accounting Return (AAR)
- Internal Rate of Return (IRR)
- **Profitability Index (PI) p119**

**Question No: 20 ( Marks: 1 ) - Please choose one**

**Which of the following set of cash flows should be considered in the decision at hand?**

- Relevant Cash Flows
- **Incremental Cash Flows**
- Negative Cash Flows
- All of the given options

**Question No: 21 ( Marks: 1 ) - Please choose one**

**\_\_\_\_\_ Cost is an outlay that has already occurred and hence is not affected by the decision under consideration.**

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• **Sunk**

- Opportunity
- Fixed
- Variable

<http://books.google.com.pk/books?id=jEaW-CReqZkC&pg=PA425&lpg=PA425&dq=Cost+is+an+outlay+that+has+already+occurred+and+hence+is+not+affected+by+the+decision+under+consideration&source=bl&ots=eD40CvHcwF&sig=Bj7AiOwKA8WQG7hgmErrBocKJus&hl=en&sa=X&ei=kZP5T6qvJ4SH4gS71oH7Bg&ved=0CDgQ6AEwAA#v=onepage&q=Cost%20is%20an%20outlay%20that%20has%20already%20occurred%20and%20hence%20is%20not%20affected%20by%20the%20decision%20under%20consideration&f=false>

**Sunk Costs**

A **sunk cost** is an outlay that has already occurred, hence is not affected by the decision under consideration. Since sunk costs are not incremental costs, they

**Question No: 22 ( Marks: 1 ) - Please choose one**

The overall (weighted average) cost of capital is composed of a weighted average of :

- The cost of common equity and the cost of debt
- The cost of common equity and the cost of preferred stock
- The cost of preferred stock and the cost of debt
- **The cost of common equity, the cost of preferred stock, and the cost of debt**

<http://wps.pearsoned.co.uk/wps/grader>

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**Question#2**

**CORRECT**

The overall (weighted average) cost of capital is composed of a weighted average of \_\_\_\_\_.

**Your Answer:** the cost of common equity, the cost of preferred stock, and the cost of debt

**Question No: 23 ( Marks: 1 ) - Please choose one**

Over the past four years, a company has paid dividends of Rs. 1.00, Rs. 1.10, Rs. 1.20 and Rs. 1.30 respectively. This pattern is expected to continue into the future. This is an example of a company pay a dividend that grows:

- **By 10 percent each year**
- At a constant rate
- By a decreasing amount
- At a decreasing rate

**Question No: 24 ( Marks: 1 ) - Please choose one**

Which of the following statement is **INCORRECT** regarding Average Accounting Return?

- AAR is a rate that makes the NPV equal to zero
- AAR is a measure of accounting profit relative to book value

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- **An investment is acceptable if its AAR is greater than a benchmark AAR**  
**p119**
- None of the given options

• **Average Accounting Return**

- AAR is a measure of accounting profit relative to book value
- AAR rule is to take an investment if its AAR exceeds a benchmark AAR

**Question No: 25 ( Marks: 1 ) - Please choose one**

**Which of the following M&M propositions states that it is completely irrelevant how a firm chooses to arrange its finances ?**

- **1st proposition p153**
- 2nd proposition
- 3rd proposition
- None of the given options

**Question No: 26 ( Marks: 1 ) - Please choose one**

**SNT Corporation has a WACC of 16% (ignoring taxes). It can borrow at 9% . Assuming that SNT has a target capital structure of 75% equity and 25% debt, what will be its cost of equity ?**

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- 13.00%
- 15.23%
- **18.33% p154**
- 20.98%

$$25\%/75\%=0.33$$
$$16\%+(16\%-9\%) \times 0.33$$
$$0.16+(0.16-0.09) \times 0.33$$
$$0.16+0.0231=18.31\%$$

**Question No: 27 ( Marks: 1 ) - Please choose one**  
**Which of the following activities decreases cash ?**

- Increasing current liabilities
- **Decreasing long term debt p163**
- Decreasing fixed assets
- Increasing equity

- Activities that decrease cash (uses of cash)
- Decreasing long term debt
- Decreasing equity
- Decreasing current liabilities
- Increasing current assets other than cash
- Increasing fixed assets

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**Question No: 28 ( Marks: 1 ) - Please choose one**

**Which of the following describes how a product moves through the current asset accounts ?**

- Cash Cycle
- **Operating Cycle p164**
- Current Cycle
- None of the given options

**Question No: 29 ( Marks: 1 ) - Please choose one**

**Which of the following is the time between sale of inventory and collection of receivables ?**

- Inventory period
- **Accounts receivable period p164**
- Collection period
- Accounts payable period

**Question No: 30 ( Marks: 1 ) - Please choose one**

**Suppose you have Rs. 10,000 on deposit. One day, you write a cheque for Rs. 2,000 and deposit Rs. 4,000. What is your disbursement float ?**

- Rs. 4,000
- + Rs. 2,000
- **Rs. 2,000**
- + Rs. 4,000

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Disbursement Float = Firm's available balance – Firm's book balance **p178**

**Question No: 31 ( Marks: 1 ) - Please choose one**

Suppose you have Rs. 70 in stock A and Rs. 120 in another stock B in your portfolio. Stock A has an expected return of 25% and stock B has an expected return of 20%. What will be the portfolio expected return ?

- 18.27%
- **21.84% p137**
- 22.50%
- 25.13%

Portfolio expected return can be calculated as:

$$\begin{aligned} \bullet E(R_p) &= 0.50 \times E(R_L) + 0.50 \times E(R_U) \\ &= 0.50 \times 25\% + 0.50 \times 20\% \\ &= 22.5\% \end{aligned}$$

• Suppose we had n assets in our portfolio, where n is any number, and let  $x_i$  stand for percentages of out money in asset  $i$ , then the expected return is:

$$E(R_p) = x_1 \times E(R_1) + x_2 \times E(R_2) + \dots + x_n \times E(R_n)$$

**Question No: 32 ( Marks: 1 ) - Please choose one**

Which of the following statement(s) is (are) true regarding Return on Investment?

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- One of the responsibilities of the financial manager is to assess the value of the proposed investment
- The return consists of income earned and capital gain
- The dollar returns are the sum of the cash received and the change in dollar value of the asset
- **All of the given options**

**Question No: 33 ( Marks: 1 ) - Please choose one**

**The MC Inc. purchased a share of common stock exactly one year ago for Rs. 45. During the past year the common stock paid an annual dividend of Rs. 2.40. The firm sold the stock today for Rs. 80. What is the rate of return the firm has earned?**

- 5.3%
- 194.2%
- **83.11% p131&132**
- 94.2%

**The correct answer: 83.11%.**

**Return is over the two-year period and includes both dividends and capital gains. Return = [(\$2.40) + (\$80 - \$45)] / \$45 = 83.11%**

You pay 45  
you sell it for 80  
you made 2.40 in dividends

Always remember the simple rate of return formula as New - Old / Old  
New is the amount you made for holding the stock, 80 + 2.40.  
Old is what you paid for it = 45  
82.40 - 45 / 45 = 83.11%

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**Question No: 34 ( Marks: 1 ) - Please choose one**

**What will be the cash inflow if we have sales of Rs. 400,000 and accounts receivable are increased by Rs. 70,000?**

- Rs. 70,000
- Rs. 230,000
- **Rs. 330,000 p125**
- Rs. 470,000

• We had sales of \$500, while accounts receivable rose by \$30 over the year, so cash inflow is \$500 – 30 = \$470

**Rules (operating activities)**

- Decrease in non-cash current assets are added to net income
- Increase in non-cash current asset are subtracted from net income
- Increase in current liabilities are added to net income
- Decrease in current liabilities are subtracted from net income
- Expenses with no cash outflows are added back to net income (depreciation and/or amortization expense are the only operating items that have no effect on cash flows in the period)
- Revenues with no cash inflows are subtracted from net income
- Non operating losses are added back to net income
- Non operating gains are subtracted from net income

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**Question No: 35 ( Marks: 1 ) - Please choose one**

**What will be the cash inflow if we have sales of Rs. 300,000 and accounts receivable are decreased by Rs. 70,000?**

- Rs. 70,000
- Rs. 230,000
- **Rs. 370,000 p125**
- Rs. 470,000

• We had sales of \$500, while accounts receivable rose by \$30 over the year, so cash inflow is  $\$500 - 30 = \$470$

**Rules (operating activities)**

- Decrease in non-cash current assets are added to net income
- Increase in non-cash current asset are subtracted from net income
- Increase in current liabilities are added to net income
- Decrease in current liabilities are subtracted from net income
- Expenses with no cash outflows are added back to net income (depreciation and/or amortization expense are the only operating items that have no effect on cash flows in the period)
- Revenues with no cash inflows are subtracted from net income
- Non operating losses are added back to net income
- Non operating gains are subtracted from net income

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**Question No: 36 ( Marks: 1 ) - Please choose one**

**Suppose a firm borrows Rs. 800,000 at 7%. What will be the total interest bill per year if tax rate is 34% ?**

- Rs. 19,040
- **Rs. 36,960 p144**
- Rs. 56,000
- Rs. 800,000

$$800000 * 7\% = 56000 * 34\% = 19040, 56000 - 19040 = 36960$$

- Suppose a firm borrows a \$1 million at 9%. Tax rate is 34%
- The total interest bill will be \$90,000 per year. This amount is tax deductible, so the \$90,000 reduces the tax bill by  $0.34 \times \$90,000 = \$30,600$
- The after-tax interest bill is thus  $\$90,000 - \$30,600 = \$59,400$
- The after-tax interest rate is  $\$59,400 / 1 \text{ million} = 5.94\%$

**Question No: 37 ( Marks: 1 ) - Please choose one**

**Which one of the following motives refers to the need for holding cash as a safety margin to act as a financial reserve?**

- speculative motive

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- Transaction motive
- **Precautionary motive p176**
- Personal motive

**Question No: 38 ( Marks: 1 ) - Please choose one**

**Suppose market value exceeds book value by Rs. 225,000. What will be the aftertax proceeds if there is a tax rate of 34 percent?**

- Rs. 105,600
- **Rs. 148,500 p21**
- Rs. 191,000
- Rs. 225,000

**Interest Expense (1 – Tax rate)**

**Question No: 39 ( Marks: 1 ) - Please choose one**

**Suppose you have bought 100 shares of a corporation one year ago at Rs. 18 per share. Over the last year, you have received a dividend of Rs. 2 per share. At the end of the year, the stock sells for Rs. 27. As per given information, what will be the capital gains yield?**

- 15%
- 25%
- 35%
- **50% p132**

**•Dividend yield = Dividend / beginning price**

**•Capital gains yield = (ending price – beginning price) / beginning price**  
**= (2700 – 1800)/1800 = 50%**

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Percentage return = Dividend yield + Capital gain yield

**Question No: 40 ( Marks: 1 ) - Please choose one**  
SNT Company purchased a vehicle for Rs. 450,000. Based on historical averages, this vehicle is worth 25% of the purchase price now and it is being sold at this price. What is the vehicle's market value ?

- Rs. 14,875
- **Rs. 112,500 (450000\*25%)**
- Rs. 337,500
- Rs. 230,000

**Question No: 41 ( Marks: 1 ) - Please choose one**  
Standard deviations for Investment A and Investment B are 19% and 28% respectively. This indicates that:

- Investment A is more volatile than Investment B
- Investment A is equally volatile to Investment B
- Investment B is less volatile than Investment A
- **Investment B is more volatile than Investment A**

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**Question No: 42 ( Marks: 1 ) - Please choose one**

**Which of the following statement is INCORRECT regarding financial leverage ?**

- Financial leverage can dramatically alter the payoffs to the shareholders.
- Financial leverage refers to the extent to which a firm relies on the debt.
- **Financial leverage must affect the overall cost of capital in any condition.**
- **P149**
- Financial leverage may not affect the overall cost of capital.

<http://studentoffortune.com/question/1567185/select-of-the-following-statement-is-INCORRECT-regarding-financial-leverage->

**Question No: 43 ( Marks: 3 )**

**What is the difference between dealer and broker ?**

**Question No: 44 ( Marks: 3 )**

**What does Static Theory of Capital Structure state?**

**Question No: 45 ( Marks: 3 )**

**Suppose there is an expected rate of 20%. What will be the risk premium if risk free rate is (i) 8% and (ii) 12% ?**

**Question No: 46 ( Marks: 5 )**

**What is the difference between Leverage and Un-levering?**

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**Question No: 47 (Marks: 5)**

Match the capital budgeting techniques are given in Column A to the criteria in Column B. Provide the correct answer in Column C.

Column A	Column B	Column C
Net Present Value	Discounted Cash Flow Criteria	
Average Accounting Return	Payback Criteria	
Payback Period	Discounted Cash Flow Criteria	
Internal Rate of Return	Accounting Criteria	
Profitability Index	Discounted Cash Flow Criteria	

**Question No: 48 (Marks: 10)**

Each of the following mutually exclusive investment projects involves an initial outlay of Rs. 240,000. The company's required rate of return is 11 percent. The estimated net cash flows for the projects are as follows:

Year	Cash Flows (Rs.)	
	Project A	Project B
1	140,000	20,000
2	80,000	40,000
3	60,000	60,000
4	20,000	100,000
5	20,000	180,000

**From the given information, find out:**

(i) inventory period

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- (ii) Accounts receivable period
- (iii) Accounts payable period
- (iv) Operating cycle
- (v) Cash cycle

**FINALTERM EXAMINATION**

Fall 2008

ACC501- Business Finance (Session - 1)

Marks: 81

**Question No: 1 ( Marks: 1 ) - Please choose one**

The accounting definition of income is:

Income = Current Assets - Current Liabilities

Income = Fixed Assets - Current Assets

Income = Revenues - Current Liabilities

**Income = Revenues - Expenses**

**Question No: 2 ( Marks: 1 ) - Please choose one**

What would be the capital spending for an organization who has purchased fixed assets of Rs.200,000 and sold fixed assets of Rs.45,000?

Rs. 245,000

Rs. 200,000

**Rs. 155,000**

Rs. 45,000

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**Question No: 3 ( Marks: 1 ) - Please choose one**

Selected information from SNT Company's accounting records is as follows:

- o Cash paid to retired common shares Rs. 15,000
- o Proceeds from issuance of preferred shares Rs. 20,000
- o Cash dividends paid Rs. 8,000
- o Proceeds from sale of equipment Rs. 25,000

On its cash flow statement for the year, SNT Company should report net cash flow from financing activities as:

- Rs. 3,000 net cash inflow
- Rs. 3,000 net cash outflow
- Rs. 8,000 net cash inflow
- Rs. 8,000 net cash inflow

**Rules (financing activities)**

Finding the Cash Flows from Financing Activities is much more intuitive and needs little explanation. Generally, the things to account for are financing activities:

- Include as outflows, reductions of long term notes payable (as would represent the cash repayment of debt on the balance sheet)
- Or as inflows, the issuance of new notes payable
- Include as outflows, all dividends paid by the entity to outside parties
- Or as inflows, dividend payments received from outside parties
- Include as outflows, the purchase of notes stocks or bonds
- Or as inflows, the receipt of payments on such financing vehicles. [citation needed]

In the case of more advanced accounting situations, such as when dealing with subsidiaries, the accountant must

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- Exclude intra-company dividend payments.
- Exclude intra-company bond interest. [citation needed]

**Question No: 4 ( Marks: 1 ) - Please choose one**

SNT Company has a current ratio of 3:2. Current Liabilities reported by the company are Rs.30, 000. What would be the Net Working Capital for the company?

Rs. 45,000

**Rs. 15,000**

( Rs. 45,000)

( Rs. 15,000)

**CR = CA/CL**

**3/2 = CA/30000**

**45000 = CA**

**NWC = CA - CL = 45000-30000 = 15000**

**Question No: 5 ( Marks: 1 ) - Please choose one**

Which of the following would not improve the current ratio?

**Borrow short-term to finance additional fixed assets**

Issue long-term debt to buy inventory

Sell common stock to reduce current liabilities

Sell fixed assets to reduce accounts payable

<http://wps.pearsoned.co.uk/wps/grader>

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**Question No: 6 ( Marks: 1 ) - Please choose one**

Which of the following are incorporated into the calculation of the Du- Pont Identity?

- I. Return on assets
- II. Equity Multiplier
- III. Total Assets Turnover
- IV. Profit Margin

I, II, and III only

I, III, and IV only

II, III and IV only

**I, II, III, and IV**

[http://highered.mcgraw-hill.com/sites/0072946733/student\\_view0/chapter3/multiple\\_choice\\_quiz.html](http://highered.mcgraw-hill.com/sites/0072946733/student_view0/chapter3/multiple_choice_quiz.html) Q#7

**Question No: 7 ( Marks: 1 ) - Please choose one**

The concepts of present value and future value are:

Directly related to each other

Not related to each other

Proportionately related to each other

**Inversely related to each other**

**Question No: 8 ( Marks: 1 ) - Please choose one**

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Which of the following is a special case of annuity, where the stream of cash flows continues forever?

Special Annuity  
Ordinary Annuity  
Annuity Due  
[Perpetuity p67](#)

**Question No: 9** ( Marks: 1 ) - Please choose one

Which of the following is an unsecured bond for which no specific pledge of property is made?

Mortgage  
[Debenture p79](#)  
Collateral  
Note Payable

**Question No: 10** ( Marks: 1 ) - Please choose one

Which of the following type of return refers to the percentage change in the amount of money you have?

[Nominal return p86](#)  
Real return  
Inflation return  
None of the given option

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**Question No: 11 ( Marks: 1 ) - Please choose one**

When real rate is \_\_\_\_\_, all interest rates will tend to be \_\_\_\_\_.

Low; higher

High; lower

**High; higher p88**

None of the given options

**Question No: 12 ( Marks: 1 ) - Please choose one**

Which of the following is the extra yield that investors demand on a taxable bond as a compensation for the unfavorable tax treatment?

Interest rate risk premium

Inflation risk premium

Default risk premium

**Taxability premium p90**

**Question No: 13 ( Marks: 1 ) - Please choose one**

In which type of the market, previously issued securities are traded among investors?

Primary Market

**Secondary Market**

Tertiary Market

None of the given options

**Question No: 14 ( Marks: 1 ) - Please choose one**

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Place the following items in the proper order of completion regarding the capital budgeting process.

- (I) Perform a post-audit for completed projects;
- (II) Generate project proposals;
- (III) Estimate appropriate cash flows;
- (IV) Select value-maximizing projects;
- (V) Evaluate projects.

II, V, III, IV, and I

III, II, V, IV, and I

II, III, V, IV, and I

II, III, IV, V, and I

[https://docs.google.com/viewer?a=v&q=cache:hua3PD0X0EAJ:media.wiley.com/product\\_data/excerpt/06/04705695/0470569506-](https://docs.google.com/viewer?a=v&q=cache:hua3PD0X0EAJ:media.wiley.com/product_data/excerpt/06/04705695/0470569506-)

[108.pdf+order+of+completion+regarding+the+capital+budgeting+process&hl=en&gl=pk&pid=bl&srcid=ADGEESgxIVFg5K68kJSinHxVRS8dj02uS3eGLXp0c1bX9X\\_DjAY1ge2ewduIfxKQikb8wGq4n6PmT9SBkslGE\\_7cxQeKxwHgnolhhoWsYURLzkOYQRVL11rVzWFqVs0DFwHw2cbwA3OY&sig=AHIEtbTHliP5uWq0pTyI1gaVrkIJJ5brLg\\_1](https://docs.google.com/viewer/a=v&q=cache:hua3PD0X0EAJ:media.wiley.com/product_data/excerpt/06/04705695/0470569506-108.pdf+order+of+completion+regarding+the+capital+budgeting+process&hl=en&gl=pk&pid=bl&srcid=ADGEESgxIVFg5K68kJSinHxVRS8dj02uS3eGLXp0c1bX9X_DjAY1ge2ewduIfxKQikb8wGq4n6PmT9SBkslGE_7cxQeKxwHgnolhhoWsYURLzkOYQRVL11rVzWFqVs0DFwHw2cbwA3OY&sig=AHIEtbTHliP5uWq0pTyI1gaVrkIJJ5brLg_1)

**Identify project proposals.** Develop and provide preliminary screening of project proposals.

**2. Estimate project cash flows.** Identify and estimate the incremental, after-tax cash flows for a proposed project.

**3. Evaluate projects.** Determine the financial viability of a project by evaluating the project's incremental after-tax cash flows.

**4. Select projects.** Choose the projects that best meet the selection criteria.

**5. Implement projects.** Determine the order of implementation, initiate, and track the selected projects.

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**6. Perform a post completion audit.** Periodically compare the actual cash flows for the project to the prior estimates in the capital budgeting proposal.

**Question No: 15 ( Marks: 1 ) - Please choose one**

An investment will be \_\_\_\_\_ if the IRR doesn't exceed the required return and \_\_\_\_\_ otherwise.

Accepted; rejected

Accepted; accepted

Rejected; rejected

**Rejected; accepted p109**

**IRR Rule**

**"Based on IRR rule an investment is acceptable if the IRR exceeds the required return. It should be rejected otherwise"**

**Question No: 16 ( Marks: 1 ) - Please choose one**

IRR and NPV rules always lead to identical decisions as long as:

Cash flows are conventional

Cash flows are independent

**Cash flows are both conventional and independent p110**

None of the given options

• IRR and NPV rules always lead to identical decisions as long as

• **Project's cash flows are conventional** i.e. first cash flow (initial investment) is negative and rest are positive

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• **Projects are independent** i.e. decision to accept or reject one project does not affect the decision to accept or reject any other

**Question No: 17 ( Marks: 1 ) - Please choose one**

A project whose acceptance does not prevent or require the acceptance of one or more alternative projects is referred to as :

A mutually exclusive project

**An independent project**

A dependent project

A contingent project

[http://wps.pearsoned.co.uk/ema\\_uk\\_he\\_wachowicz\\_fundfinman\\_12/26/6680/1710103.cw/content/index.html](http://wps.pearsoned.co.uk/ema_uk_he_wachowicz_fundfinman_12/26/6680/1710103.cw/content/index.html) Q#7

**Question No: 18 ( Marks: 1 ) - Please choose one**

Finding Net Present Value comes under which type of capital budgeting criteria ?

**Discounted Cash Flow Criteria** p118

Accounting Criteria

Payback Criteria

None of the given options

**Question No: 19 ( Marks: 1 ) - Please choose one**

\_\_\_\_\_ Cost is an outlay that has already occurred and hence is not affected by the decision under consideration.

**Sunk**

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Opportunity  
Fixed  
Variable

**Question No: 20 ( Marks: 1 ) - Please choose one**

Which of the following is the overall return the firm must earn on its existing assets to maintain the value of the stock ?

**WACC (Weighted Average Cost of Capital) p146**

AAR (Average Accounting Return)

IRR (Internal Rate of Return)

MIRR (Modified Internal Rate of Return)

**Question No: 21 ( Marks: 1 ) - Please choose one**

Mr. A, as a financial consultant, has prepared a feasibility report of a project for XYZ Company that the company is planning to undertake. He has suggested that the project is feasible. The consultancy fee paid to Mr. A will be considered as:

**Sunk cost**

Opportunity cost

Both sunk cost and opportunity cost

Neither sunk cost nor opportunity cost

**Question No: 22 ( Marks: 1 ) - Please choose one**

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The current price of SNT stock is Rs. 50. Dividends are expected to grow at 7 percent indefinitely and the most current dividend was Rs. 1.00. What is the required rate of return on SNT stock?

**9.00 percent p96**

9.14 percent

9.33 percent

10.65 percent

$$R = D_1/P_0 + g$$

$$= 1/50 + 0.07 = 9\%$$

<http://answers.yahoo.com/question/index?qid=20100804060644AAMtjYt>

**Question No: 23 ( Marks: 1 ) - Please choose one**

Which of the following are rights of an owner of a share of common stock for firm which has no preferred share?

The right to vote for directors

The right to share proportionately in dividend paid

The right to vote on stockholder matters of great importance

**All of the given options**

<http://answers.yahoo.com/question/index?qid=20100804060644AAMtjYt>

**Question No: 24 ( Marks: 1 ) - Please choose one**

Which one of the following typically applies to preferred stock but not to common stock?

Dividend yield

**Cumulative dividends**

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Voting rights  
Tax deductible dividends

<http://odin.lcb.uoregon.edu/aemami/318Practice/PRACTICE%207/Chpt07.htm?As4=1&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&TA99=&TA100=&TA101=&TA102=&TA103=&TA104=&TA105=&TA106=&TA107=> Q#4

**Question No: 25 ( Marks: 1 ) - Please choose one**

You must own which of the following to vote against a merger proposal from another corporation?

Preferred share  
A debenture  
**Common stock**  
Cumulative dividend stock

**Question No: 26 ( Marks: 1 ) - Please choose one**

Which of the following strategy belongs to flexible policy regarding size of investments in current assets ?

**To maintain a high ratio of current assets to sales p168**

To maintain a low ratio of current assets to sales  
To maintain less short-term debt and more long-term debt  
To maintain more short-term debt and less long-term debt

**Question No: 27 ( Marks: 1 ) - Please choose one**

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Which of the following strategy belongs to flexible policy regarding financing of current assets?

To maintain a high ratio of current assets to sales

To maintain a low ratio of current assets to sales

**To maintain less short-term debt and more long-term debt p168**

To maintain more short-term debt and less long-term debt

**Question No: 28 ( Marks: 1 ) - Please choose one**

Suppose you have Rs. 10,000 on deposit. One day, you write a cheque for Rs.2, 000 and deposit Rs. 4,000. What is your collection float?

**Rs. 4,000 p178**

+ Rs. 2,000

Rs. 2,000

+ Rs. 4,000

- Suppose you have \$5,000 on deposit.
- One day, you write a cheque for \$1,000 and deposit \$2,000.
- What are your disbursement, collection and net floats?
- After writing the cheque, you show a balance of \$4,000 on your books, but bank shows \$5,000 while the cheque is clearing. So you have a disbursement float of \$1,000
- Depositing \$2,000 increases the book balance to \$6,000, but the available balance remains the same until the cheque clears. So collection float is -\$2,000.
- Net float = \$1000 + (-2,000) = -\$1,000

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**Question No: 29 ( Marks: 1 ) - Please choose one**

Suppose you have Rs. 10,000 on deposit. One day, you write a cheque for Rs. 2,000 and deposit Rs. 4,000. What is your net float?

Rs. 4,000

+ Rs. 2,000

**Rs. 2,000 p178**

+ Rs. 4,000

- Suppose you have \$5,000 on deposit.
- One day, you write a cheque for \$1,000 and deposit \$2,000.
- What are your disbursement, collection and net floats?
- After writing the cheque, you show a balance of \$4,000 on your books, but bank shows \$5,000 while the cheque is clearing. So you have a disbursement float of \$1,000
- Depositing \$2,000 increases the book balance to \$6,000, but the available balance remains the same until the cheque clears. So collection float is -\$2,000.
- Net float = \$1000 + (-2,000) = -\$1,000

**Question No: 30 ( Marks: 1 ) - Please choose one**

Which of the following is known as the group of assets such as stocks and bonds held by an investor?

Stock Bundle

**Portfolio p137**

Capital Structure

None of the given options

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**Question No: 31 ( Marks: 1 ) - Please choose one**

Which of the following is referred as the ratio of the standard deviation of a distribution to the mean of that distribution?

Probability distribution

The expected return

The standard deviation

**Coefficient of variation**

[http://en.wikipedia.org/wiki/Standard\\_deviation#Relationship\\_between\\_standard\\_deviation\\_and\\_mean](http://en.wikipedia.org/wiki/Standard_deviation#Relationship_between_standard_deviation_and_mean)

**Question No: 32 ( Marks: 1 ) - Please choose one**

The MC Inc. purchased a share of common stock exactly one year ago for Rs. 45. During the past year the common stock paid an annual dividend of Rs. 2.40. The firm sold the stock today for Rs. 80. What is the rate of return the firm has earned?

5.3%

194.2%

**83.11% p132**

94.2%

• **Dividend yield** = Dividend / beginning price

• **Capital gains yield** = (ending price – beginning price) / beginning price

• **Total percentage return** = dividend yield + capital gains yield

**The correct answer: 83.11%.**

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**Return is over the two-year period and includes both dividends and capital gains.**

**Return**

$$= [(\$2.40) + (\$80 - \$45)] / \$45 = 83.11\%$$

You pay 45

you sell it for 80

you made 2.40 in dividends

Always remember the simple rate of return formula as  $\text{New} - \text{Old} / \text{Old}$

New is the amount you made for holding the stock,  $80 + 2.40$ .

Old is what you paid for it = 45

$$82.40 - 45 / 45 = 83.11\%$$

**Question No: 33 ( Marks: 1 ) - Please choose one**

Mr. Sami has bought 50 shares of a corporation one year ago at Rs. 20 per share. Over the last year, he received a dividend of Rs. 2 per share. At the end of the year, the stock sells for Rs. 25. As per given information, what will be his total percentage return?

10 %

20 %

**35 % p132**

45 %

• **Dividend yield** = Dividend / beginning price

$$= 2 * 50 / 1000 = 0.1$$

• **Capital gains yield** = (ending price – beginning price) / beginning price

$$= (1250 - 1000) / 1000 = 25\%$$

Percentage return = Dividend yield + Capital gain yield

$$= 0.1 + 0.25 = 35\%$$

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**Question No: 34 ( Marks: 1 ) - Please choose one**

While performing the feasibility analysis for a project, an operating cash flow of Rs. 225,000 have been calculated. Net working capital has declined by Rs. 40,000. There was a net capital spending of Rs. 100,000 during the year. What will be the total cash flow for the project?

Rs. 85,000

**Rs. 165,000**

Rs. 285,000

Rs. 365,000

Operating cash flow - change in NWC – Capital spending  
 $225000 - (-40000) - 100000 = 165000$

**Question No: 35 ( Marks: 1 ) - Please choose one**

The total market value of a companies stocks is calculated as Rs. 250 million and the total market value of the companies debt are calculated as Rs.150 million. What percent of the firms financing is debt?

**37.50%**

50.00%

62.50%

70.00%

$250 / (250 + 150) * 100 = 37.50\%$

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**Question No: 36 ( Marks: 1 ) - Please choose one**

Suppose a firm borrows Rs. 800,000 at 7%. What will be the after-tax interest rate if tax rate is 34%?

3 .00 %

**4 .62 % p144**

5 .20 %

8 .00 %

$$800000 * 7\% = 56000$$

$$56000 * 34\% = 19040$$

$$56000 - 19040 = 36960$$

$$36960 / 800000 = 4.62\%$$

$$R_D \times (1 - T_c).$$

$$\bullet \text{So } 9\% \times (1 - 0.34) = 5.94\%$$

• Suppose a firm borrows a \$1 million at 9%. Tax rate is 34%

• The total interest bill will be \$90,000 per year. This amount is tax deductible, so the \$90,000 reduces the tax bill by  $0.34 \times \$90,000 = \$30,600$

• The after-tax interest bill is thus  $\$90,000 - \$30,600 = \$59,400$

• The after-tax interest rate is  $\$59,400 / \$1 \text{ million} = 5.94\%$

**Question No: 37 ( Marks: 1 ) - Please choose one**

Opportunity losses from having inadequate inventory are termed as:

Carrying costs

Opportunity costs

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20%

33%

40%

**67%**

•WACC is calculated as

$$WACC = (E/V) \times R_E + (D/V) \times R_D \times (1 - T_c)$$

Where

- $T_c$  is the corporate tax rate,
- E is the market value of the firm's equity,
- D is the market value of the firm's debt
- $V = E + D$ .
- E/V is the percentage of the firm's financing that is equity
- D/V is the percentage that is debt.

**Question No: 41 ( Marks: 1 ) - Please choose one**

The book value of a system is Rs. 50,350 at the end of year 3 of its life. What will be the total after-tax cash flow from sale if we sell this system for Rs. 30,000 at this time? (Tax rate is 34%)

Rs. 20,350

Rs. 30,919

**Rs. 36,919 p128**

Rs. 80,350

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$$50350 - 30000 = 20350 * 34\% = 6919 + 30000 = 36919$$

• The book value at the end of year 4 is \$27,648. If we sell the system for \$10,000 at that time, we will have a loss of \$17,648 for tax purposes.

• We get \$10,000 from buyer

• We save  $0.34 \times \$17,648 = \$6,000$  in taxes. So the total after tax cash flow from the sale is a \$16,000 cash inflow

**Question No: 42 ( Marks: 1 ) - Please choose one**

What will be the variance if standard deviation for the returns of an investment is 0.2829 ?

**0.0800**

0.0892

0.5319

Cannot be estimated without more information

$$0.2829^2 = 0.0800$$

**Question No: 43 ( Marks: 3 )**

Write down the components of total return in terms of dividend growth model.

**Question No: 44 ( Marks: 3 )**

What is the difference between operating cycle and cash cycle?

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**Question No: 45 ( Marks: 3 )**

How a firms overall cost of capital is calculated?

**Question No: 46 ( Marks: 5 )**

Define the following terms:

- (i) Dealer
- (ii) Broker
- (iii) Bid Price
- (iv) Strike Price
- (v) Spread

**Question No: 47 ( Marks: 5 )**

A firm has a total value of Rs. 1 million and debt valued at Rs. 400,000. What is the after-tax weighted average cost of capital if the cost of debt is 12%, the cost of equity is 15% and tax rate is 35% ?

**Question No: 48 ( Marks: 10 )**

SNT & Co. has the following Target capital structure:

Debentures = Rs. 5.00 Billion  
Preferred shares = Rs. 2.65 Billion  
Common shares = Rs. 9.35 Billion

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Total = Rs. 17 Billion

Bonds carry an interest rate of 11.5%. Common stocks and Preferred stocks have a return of 15.50 % and 12% respectively and corporate tax rate is 40%. Compute the present Weighted Average Cost of Capital (WACC) for SNT & Co.

**Question No: 49 ( Marks: 10 )**

Standard Manufacturing Company (SMC) needs one of two machines. Machine X costs Rs. 25,000 and has cash flows of Rs. 8,000 a year for six years. Machine Y costs Rs. 30,000 and has cash flows Rs.7,000 a year for six years. SMC has 12% cost of capital. Calculate each machine Payback Period and NPV (Net Present Value) and evaluate the results.

**FINAL TERM EXAMINATION**

Fall 2008

ACC501- Business Finance (Session - 1)

Marks: 81

**Question No: 1 ( Marks: 1 ) - Please choose one**

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Which of the following is the difference between current assets and current liabilities?

- Surplus Asset
- Short-term Ratio
- Working Capital**
- Current Ratio

**Question No: 2 ( Marks: 1 ) - Please choose one**

A business owned by a single person is known as:

- Sole-proprietorship**
- General partnership
- Limited partnership
- Corporation

**Question No: 3 ( Marks: 1 ) - Please choose one**

In a common-size balance sheet, all items are shown as a percentage of:

- Total Assets**
- Total Liabilities
- Total Owner s Equity
- None of the given options

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<http://www.accounting-world.com/2011/04/common-size-balance-sheet.html>

### Common Size Balance Sheet

A balance sheet that report its items (assets, liabilities and equity) as the percentage of Total assets (not report in dollars). Each item of the balance sheet is percentage of total assets of an organization

**Question No: 4 ( Marks: 1 ) - Please choose one**

A company's ability to meet long-term obligations can be estimated by using which of the following set of ratios?

Liquidity Ratio

**Solvency Ratios p34**

Asset Management Ratios

Market Value Ratios

**Question No: 5 ( Marks: 1 ) - Please choose one**

According to Du Pont Identity, ROE is affected by which of the following?

Operating efficiency

Asset use efficiency

Financial Leverage

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**All of the given options**

**Question No: 6 ( Marks: 1 ) - Please choose one**

Which of the following is a series of constant cash flows that occur at the end of each period for some fixed number of periods?

**Ordinary annuity p63**

- Annuity due
- Perpetuity
- None of the given options

**Question No: 7 ( Marks: 1 ) - Please choose one**

A portion of profits, which a company distributes among its shareholders, is known as:

**Dividends**

- Retained Earnings
- Capital Gain
- Interest

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**Question No: 8 ( Marks: 1 ) - Please choose one**

What amount a borrower would pay at the end of fourth year with a 4-year, 12%, interest-only loan of Rs. 3,000?

Rs. 360

Rs. 2,000

Rs. 3,000

**Rs. 3,360 p69**

$$3000 \times 12\% = 360$$

$$360 + 3000 = 3360$$

**Interest-Only Loans**

- Calls for the borrower to pay interest each period and to repay the entire principal at some time in the future.
- With a 3-year, 10%, interest-only loan of \$1,000, the borrower would pay  $\$1,000 \times 0.10 = \$100$  in interest at the end of first and second years,
- At the end of third year, he would return \$1000 plus the \$100 in interest for that year.

**Question No: 9 ( Marks: 1 ) - Please choose one**

A company issues bonds with a Rs. 1,000 face value. What is the coupon rate if the coupon payments of Rs. 45 are paid every 6 months?

3 percent

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6 percent

**9 percent**

12 percent

$$C = I * F$$

$$45 * 2 = 90$$

$$90 = I * 1000$$

$$I = 90 / 1000 = 9\%$$

**Question No: 10 ( Marks: 1 ) - Please choose one**

Given two bonds identical but for maturity, the price of the longer-term bond will change \_\_\_\_\_ that of the shorter-term bond, for a given change in market interest rates.

**More than p77**

Less than

Equal to

None of the given options

**Question No: 11 ( Marks: 1 ) - Please choose one**

When corporations borrow, they generally promise to:

- I. Make regular scheduled interest payments
- II. Give the right of voting to bondholders
- III. Repay the original amount borrowed (principal)

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IV. Give an ownership interest in the firm

I and II

**I and III**

II and IV

I, III, and IV

**Question No: 12 ( Marks: 1 ) - Please choose one**

Which of the following allows a company to repurchase part or all of the bond issue at a stated price?

Repayment

Seniority

**Call provision p80**

Protective covenants

**Question No: 13 ( Marks: 1 ) - Please choose one**

Sumi Inc. has policy of paying a Rs. 9 per share dividend every year. If this policy is to continue indefinitely, what will be the value of a share of stock at a 12% required rate of return?

Rs. 30

Rs. 45

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Rs. 60

**Rs. 75 p91**

**9/0.12 = 75**

• So the per share value is

$P_0 = D/R$

Where R is the required rate of return

• CVP Corporation has a policy of paying a \$10 per share dividend every year.

• If this policy is to continue indefinitely, what is the value of a share of stock if the required rate of return is 20%?

• Since the stock amounts to be a perpetuity, value of the share is

□  $\$10/0.20 = \$50$  per share

**Question No: 14 ( Marks: 1 ) - Please choose one**

In which type of the market, previously issued securities are traded among investors?

Primary Market

**Secondary Market**

Tertiary Market

None of the given options

**Question No: 15 ( Marks: 1 ) - Please choose one**

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An investment should be accepted if the net present value is \_\_\_\_\_ and rejected if it is \_\_\_\_\_.

Positive; positive

**Positive; negative p105**

Negative; negative

Negative; positive

**“An investment should be accepted if the net present value is positive and rejected if it is negative.”**

**Question No: 16 ( Marks: 1 ) - Please choose one**

The XYZ Corporation is considering an investment that will cost Rs. 80,000 and have a useful life of 4 years. During the first 2 years, the net incremental after-tax cash flows are Rs. 25,000 per year and for the last two years they are Rs. 20,000 per year. What is the payback period for this investment?

**1 to 62mcqs =62 marks**

**63 to 65 subjective=3\*3 =9marks**

**66to 69 subjective=5\*4 =20marks**

**Total paper 91 marks**

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1. The time between sale of inventory and collection of receivable.

a account receivable

b operation cycle

c inventory period

**d none of above p164**

**Accounts receivable period**

• The time between sale of inventory and collection of receivable. (here, it is 45 days)

2. Allow a bank to substitute its creditworthiness for the customer, for a fee is called\_\_\_\_\_ -

a open bank account

b commercial draft

c promisory note

**d banker acceptance p185**

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•**Banker's acceptances** allow a bank to substitute its creditworthiness for the customer, for a fee.

3. Standard deviations for Investment A and Investment B are 25% and 12% respectively. This indicates that :

Select correct option:

Investment A is less volatile than Investment B

Investment B is equally volatile to Investment A

**Investment A is more volatile than Investment B**

Investment B is more volatile than Investment A

4. find the average 2%, 5%, 6%, 8%

a 5%

**b 5.25 %**

c 6%

d 8%

5 what is standard deviation of this averages 2%, 5%, 7%

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6. As the dividend is always same for a zero growth stock, so the stock can also be viewed as

7. Which of the following statement shows revenue, expense, and net worth as of a specific date?

a balance sheet

**b income statement**

c cashflow

d none of above

8. which of the following character is not a systematic risk

market risk

interest risk

inflation risk

**strike call in a company**

9. A company has a two director and 1 shareholder which have 25 power of share the voter for director is

a 100

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b150

**c50**

d25

10. An investment will be \_\_\_\_\_ if the IRR doesn't exceed the required return and \_\_\_\_\_ otherwise.

Select correct option:

Accepted; rejected

Accepted; accepted

Rejected; rejected

**Rejected; accepted p109**

**IRR Rule**

**"Based on IRR rule an investment is acceptable if the IRR exceeds the required return. It should be rejected otherwise"**

11. Which of the following is the overall return the firm must earn on its existing assets to maintain the value of the stock?

Select correct option:

IRR (Internal Rate of Return)

MIRR (Modified Internal Rate of Return)

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**WACC (Weighted Average Cost of Capital) p146**

AAR (Average Accounting Return)

•The WACC is the overall return the firm must earn on its existing assets to maintain the value of the stock.

12. Which of the following is the return that firm's creditors demand on new borrowings ?

Select correct option:

**Cost of debt p143**

Cost of preferred stock

Cost of common equity

Cost of retained earnings

13. In which type of projects, the unequal lives of the projects do affect the analysis ?

Select correct option:

Mutually exclusive

Dependent

**Independent**

Correlated

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14. Mr. Naveed has bought 100 shares of a corporation one year ago at Rs. 23 per share. Over the last year, he received a dividend of Rs. 1.50 per share. At the end of the year, the stock sells for Rs. 31. As per given information, what will be his total percentage return ?

Select correct option:

10.63%

20.20%

35.12%

**41.30%**

• **Dividend yield** = Dividend / beginning price

• **Capital gains yield** = (ending price – beginning price) / beginning price

Percentage return = Dividend yield + Capital gain yield

$$= 6.5\% + 34.8\% = 41.3\%$$

15. Which of the following is known as the group of assets such as stocks and bonds held by an investor ?

Select correct option:

Stock Bundle

**Portfolio p137**

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Capital Structure  
None of the given options

16. Suppose the initial investment for a project is Rs. 16 million and the cash flows are Rs. 4 million in the first year and Rs. 9 million in the second and Rs. 5 million in the third. The project will have a payback period of:  
Select correct option:

**2.6 Years**

3.1 Years

3.7 Years

4.1 Years

Payback Period = Years before recovery + (Uncovered Cost / Cash Flow from which the cost is to be covered)

17. Find the cash cycle. Inventory period is 38 days account payable period is 50 days and average account receivable period is 30 days

a.68

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**b 18**

c 80

d 118

Operating cycle = Inventory period + Receivable period

$$38 + 30 = 68$$

Cash cycle = Operating cycle – Accounts payable period

$$68 - 50 = 18$$

Question 63= operating cash flow of Rs. 200,000. Net working capital has decreased by Rs. 50,000 and there is a net capital spending of Rs. 0 during the year. Calculate total cash flow. (3marks)

Solution:

Total cash flow=200000-(-50000)

total cash flow =250,000

Question 64= snk company find the profitability index dividend 2 and price= 200 (3marks)

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solution=  $2/200=0.01=1$  answer

question 65=3marks

question 66= define systematic risk and unsystematic risk and also define which risk is eliminated by diversification 5 marks

Question 67= which issue cover in finance and investment area 5marks

question 68= credit policy and its component 5marks

question 69= define optimal policy 5marks

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	ACC501 - BUSINESS FINANCE (Session - 3 )	Time: 150min
StudentID/LoginID:	_____	
Student Name:	_____	
Center Name/Code:	_____	
Exam Date:	Wednesday, July 11, 2007	
<b>Please read the following instructions carefully before attempting any question:</b>		
<ul style="list-style-type: none"><li>● All questions are compulsory.</li><li>● This exam consists of <b>10</b> Multiple Choice Questions (MCQ's), <b>5</b> True/False Questions, <b>3</b> Short Questions and <b>3</b> Numerical Questions.</li><li>● <b>Question No. 1-10</b> are MCQs carrying <b>1</b> Mark each, <b>Question No. 11-15</b> are True/False Questions carrying <b>1</b> Mark each, <b>Question No.16-18</b> are short questions carrying <b>5</b> Marks each and <b>Question No. 19-21</b> are numerical questions carrying <b>10</b> Marks each.</li><li>● For each MCQ, read the choices available carefully and select the choice which you consider is the correct one.</li><li>● You are required to show all the working of short questions as well as Numerical questions.</li><li>● The use of calculator and financial tables is allowed.</li><li>● The use of mobile phones in exam center is strictly prohibited.</li></ul>		

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- A clock has been given in the exam software. Software will automatically be closed after 150 minutes.
- Remember do not spend too much time on any one MCQ. Since all MCQ's carry equal marks, it is important to manage your time and responses to test questions effectively.
- This Examination is closed book, closed notes and closed neighbours.
- Failure to comply with the supervisor's directions will result in your test being cancelled. Please comply with supervisor's directions to avoid any unpleasant event.

For Teacher's use only											
Question	1	2	3	4	5	6	7	8	9	10	Total
Marks											
Question	11	12	13	14	15	16	17	18	19	20	
Marks											
Question	21										
Marks											

Question No: 1 ( Marks: 1 ) - Please choose one

The process of planning and managing a firm's long-term investments is called :

- ▶ Planning Process
- ▶ Capital Structure
- ▶ **Capital Budgeting p4**

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- ▶ Managing Process

Question No: 2 ( Marks: 1 ) - Please choose one

Return on Equity (ROE) = \_\_\_\_\_ x Total Assets Turnover x Equity Multiplier

- ▶ **Profit Margin p45**
- ▶ Total Sales
- ▶ Net Income
- ▶ Total Equity

Question No: 3 ( Marks: 1 ) - Please choose one

If a bank loans out Rs. 10,000 for 90 days at 8% simple interest, the Present Value (PV) will be :

- ▶ Rs. 9,105
- ▶ **Rs. 9,807 p55**

$$\begin{aligned} PV &= 10000 / [1 + (.08)(90/365)] \\ &= 10000 / 1.019726 \\ &= \$9,806.56 \end{aligned}$$

- ▶ Rs. 10,325

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▶ Rs. 10,765

Question No: 4 ( Marks: 1 ) - Please choose one

The \_\_\_\_\_ is the rate where NPV (Net Present Value) equals to zero.

- ▶ WACC (Weighted Average Cost of Capital)
- ▶ **IRR (Internal Rate of Return)**
- ▶ MIRR (Modified Internal Rate of Return)
- ▶ AAR (Average Accounting Return)

Question No: 5 ( Marks: 1 ) - Please choose one

\_\_\_\_\_ is adopted to permit minority participation.

- ▶ **Cumulative Voting p98**
- ▶ Straight Voting
- ▶ Proxy Voting
- ▶ Staggering

Question No: 6 ( Marks: 1 ) - Please choose one

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Which one of the following statements projects future years' operations in a summarized format ?

- ▶ Income Statement
- ▶ Cash Flow Statement
- ▶ **Pro Forma Financial Statement** p121
- ▶ None of the given options

Question No: 7 ( Marks: 1 ) - Please choose one

The direct and indirect costs associated with going bankrupt or experiencing financial distress, are known as :

- ▶ Direct Bankruptcy Costs
- ▶ Indirect Bankruptcy Costs
- ▶ **Financial Distress Costs** p158
- ▶ All of the given options

Question No: 8 ( Marks: 1 ) - Please choose one

Suppose you bought 1,500 shares of a corporation at Rs. 25 each. After a year, you received Rs. 3,000 (Rs. 2 per share) in dividends. The dividend yield will be :

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▶ 5.00 %

▶ **8.00%**

$$\begin{aligned}\text{Dividend yield} &= \text{Dividend} / \text{beginning price} \\ &= 3000 / (1500 * 25) \\ &= 8\%\end{aligned}$$

▶ 10.00%

▶ 12.00%

Question No: 9 ( Marks: 1 ) - Please choose one

You earn a 7% real return. If the inflation rate is 5 percent, what is your nominal return ?

▶ 8.96 %

▶ 9.05 %

▶ 11.65 %

▶ **12.35%**

$$1 + R = (1 + r) \square (1 + h)$$

$R$  = the nominal return  
 $r$  = the real return  
 $h$  = the inflation rate

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$$1 + R = (1+0.07)^*(1+0.05)$$
$$R = 12.35\%$$

Question No: 10 ( Marks: 1 ) - Please choose one

The projected cash flows from a project are :

Years	Cash flows
1	Rs. 100
2	Rs. 300
3	Rs. 600
4	Rs. 800

The project costs Rs. 1,000. What would be the payback period for the project ?

- ▶ 2.00 Years
- ▶ 2.67 Years
- ▶ **3.00 Years**

Payback Period = Years before recovery + (Uncovered Cost / Cash Flow from which the cost is to be covered)

- ▶ 3.67 Years

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Question No: 11 ( Marks: 1 ) - Please choose one

Sole Proprietorship is a business created as a distinct legal entity owned by one or more individuals or entities.

- ▶ True
- ▶ **False p8**

**Corporation**

A business created as a distinct legal entity owned by one or more individuals or entities.

Question No: 12 ( Marks: 1 ) - Please choose one

The term discounting is associated with Future Value concept whereas the term compounding is associated with Present Value concept.

- ▶ True
- ▶ **False**

Question No: 13 ( Marks: 1 ) - Please choose one

Constant Growth Stock is a share of common stock in a company with a constant rate of dividend.

- ▶ **True**
- ▶ False

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Question No: 14 ( Marks: 1 ) - Please choose one

Portfolio is the group of assets (stocks and bonds) held by an investor.

▶ **True p137**

▶ False

Question No: 15 ( Marks: 1 ) - Please choose one

The difference between bank cash and book cash, representing the net effect of cheques in the process of clearing is called float.

▶ **True p178**

▶ False

Question No: 16 ( Marks: 5 )

Following are given cash inflows of a project. Assume that all cash flows are received at the end of the period.

Period	Cash Flows
1	Rs.10,000
2	Rs.15,000

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3	Rs.20,000
4	Rs.30,000
5	Rs.35,000

Calculate the future value of cash flows stream at the end of year 5 with a compound annual interest rate of 10%.

Question No: 17 ( Marks: 5 )

Write down the statements for the followings:

- a. NPV (Net Present Value) Rule
- b. IRR (Internal Rate of Return) Rule
- c. Payback Rule
- d. PI (Profitability Index) Rule
- e. AAR (Average Accounting Return) Rule

Question No: 18 ( Marks: 5 )

What do M&M Proposition I and Proposition II state ?

Question No: 19 ( Marks: 10 )

Mr. Jamil has Rs. 70,000 that he can deposit in savings accounts of any of three banks A, B or C for a three years period. Bank A compounds interest on annual basis; Bank B compounds interest semi-annually (twice each year); and Bank C compounds interest quarterly (four times each year). All three banks have a stated annual interest rate of 12%.

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1. How much Mr. Jamil will have in his account after three years if he deposits his money in Bank A ?
2. How much He will have in his account after three years if he deposits his money in Bank B ?
3. How much He will have in his account after three years if he deposits his money in Bank C ?
4. On the basis of your findings in above parts, describe which bank should Mr. Jamil deal with and why ?

Question No: 20 ( Marks: 10 )

SNT Company presently paid a dividend of Rs.1.5 per share and has a share price of Rs.25. The dividends are expected to grow @ 15% forever. SNT Company has Rs.100 million in equity and Rs.75 million in debt in its total capital. The tax rate for the firm is 35% and the Cost of debt is 12%. Calculate the Weighted Average Cost of Capital (WACC) for SNT Company?

Question No: 21 ( Marks: 10 )

Magi Inc. specializes in toys and receives all income from sales.

Quarters *	1	2	3	4	1 (next year)
Sales (Rs.)	500,000	600,000	650,000	800,000	550,000

\* Each quarter consists of 3 months (90 days)

- Accounts Receivable:
  - Beginning receivables = Rs. 250,000
  - Average Collection Period = 30 days

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- Accounts Payable:
  - Purchases = 50 % of next quarter's sales
  - Beginning payables = Rs. 125,000
  - Accounts Payable Period is 45 days
- Other expenses:
  - Wages, taxes and other expenses are 25% of sales
  - Interest and dividend payments are Rs. 50,000
  - A major capital expenditure of Rs. 200,000 is expected in the second quarter

You are just required to calculate the Cash Collections (Receipts) and Cash Disbursements (Payments) for four Quarters.

Question No: 1 ( Marks: 1 ) - Please choose one

A series of constant, or level, cash flows that occur at the end of each period for some fixed number of periods is called a/an:

- ▶ Present Value

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- ▶ Future Value
- ▶ **Ordinary Annuity p63**
- ▶ Ordinary Share

Question No: 2 ( Marks: 1 ) - Please choose one

The Ratios showing the ability of a firm to pay its bills in short-run are called:

- ▶ Leverage Ratios
- ▶ **Liquidity Ratios p34**
- ▶ Profitability Ratios
- ▶ Market Value Ratios

Question No: 3 ( Marks: 1 ) - Please choose one

GAAP stands for:

- ▶ **Generally Accepted Accounting Principles**
- ▶ Generally All-rounder Accounting Principles
- ▶ General Accepting Accounts Principles

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- ▶ None of the given options

Question No: 4 ( Marks: 1 ) - Please choose one

A contract between the bond issuer and bond holder is called:

- ▶ **Bond Indenture p78**
- ▶ Bond Debenture
- ▶ Bond Value
- ▶ None of the given options

Question No: 5 ( Marks: 1 ) - Please choose one

Suppose you have a portfolio comprised of two securities X and Y. In the portfolio, 60 shares are of stock X valued at Rs.10 per share and 40 shares are of stock Y valued at Rs.3 per share. What is the approximate weight of stock X in the portfolio?

- ▶ 23 %
- ▶ 40 %
- ▶ **60 %**
- ▶ 83 %

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Question No: 6 ( Marks: 1 ) - Please choose one

In which market, previously issued securities are traded among investors?

- ▶ Primary Market
- ▶ **Secondary Market p100**
- ▶ Tertiary Market
- ▶ None of the given options

Question No: 7 ( Marks: 1 ) - Please choose one

Which of the following is the present value of a series of future net cash flows that will result from an investment, minus the amount of the original investment?

- ▶ Present Value
- ▶ Future Value
- ▶ **Net Present Value**
- ▶ Terminal Value

Question No: 8 ( Marks: 1 ) - Please choose one

You earn a 5 percent real return. If the inflation rate is 4 percent, what is your nominal return?

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▶ 8.96 %

▶ 9.05 %

▶ **9.20 %**

[http://highered.mcgraw-hill.com/sites/0073405132/student\\_view0/chapter6/chapter\\_quiz.html#question\\_14](http://highered.mcgraw-hill.com/sites/0073405132/student_view0/chapter6/chapter_quiz.html#question_14)

$$1 + R = (1 + r) \square (1 + h)$$

$R$  = the nominal return

$r$  = the real return

$h$  = the inflation rate

$$1 + R = (1 + 5\%) * (1 + 4\%)$$

$$R = 9.2\%$$

▶ 9.92 %

Question No: 9 ( Marks: 1 ) - Please choose one

Fee paid to the consultant for evaluating the option of launching a new product will be considered as:

▶ **Sunk Cost p120**

▶ Opportunity Cost

▶ Financing Cost

▶ Operating Cost

Question No: 10 ( Marks: 1 ) - Please choose one

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A risk that affects a single or at most a small number of assets is called:

- ▶ **Unsystematic Risk p140**
- ▶ Unique Risk
- ▶ Diversifiable Risk
- ▶ All of the given options

Question No: 11 ( Marks: 1 ) - Please choose one

What will be the payback period of a Rs.70,000 investment with the following cash inflows?

Years	Cash flows
1	Rs. 15,000
2	Rs. 20,000
3	Rs. 25,000
4	Rs. 15,000
5	Rs. 5,000

- ▶ 3.57 years
- ▶ **3.67 years**  
Payback Period = Years before recovery + (Uncovered Cost / Cash Flow from which the cost is to be covered)
- ▶ 4.57 years

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- ▶ 4.67 years

Question No: 12 ( Marks: 1 ) - Please choose one

Which of the following is the required return on a firm's debt by its creditors?

- ▶ Cost of Equity
- ▶ Cost of Debt
- ▶ Cost of Preferred Stock
- ▶ **Cost of Capital**

Question No: 13 ( Marks: 1 ) - Please choose one

Which one of the followings is the overall required return the firm must earn on its existing assets to maintain the value of the stock?

- ▶ AAR (Average Accounting Return)
- ▶ IRR (Internal Rate of Return)
- ▶ MIRR (Modified Internal Rate of Return)
- ▶ **WACC (Weighted Average Cost of Capital) p146**

Question No: 14 ( Marks: 1 ) - Please choose one

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The costs to store and finance the assets are known as:

- ▶ **Carrying Costs p168**
- ▶ Shortage Costs
- ▶ Manufacturing Costs
- ▶ None of the given options

Question No: 15 ( Marks: 1 ) - Please choose one

The minimum level of inventory that a firm keeps on hand is called:

- ▶ Common stock
- ▶ **Safety Stock p193**
- ▶ Preferred Stock
- ▶ Dangerous Stock

Question No: 16 ( Marks: 1 ) - Please choose one

Realization Principle is one of the basic principles of GAAP.

- ▶ **True p19**

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▶ False

Question No: 17 ( Marks: 1 ) - Please choose one

Whenever the word Dividend is used, it always refers to a long-term loan.

▶ True

▶ **False**

Question No: 18 ( Marks: 1 ) - Please choose one

A preferred dividend is exactly like interest on bond.

▶ True

▶ **False p99**

Question No: 19 ( Marks: 1 ) - Please choose one

By IRR rule, take a project when its IRR exceeds the required return.

▶ **True p109**

IRR Rule

"Based on IRR rule an investment is acceptable if the IRR exceeds the required return. It should be rejected otherwise"

▶ False

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Question No: 20 ( Marks: 1 ) - Please choose one
Diversification is the group of assets such as stocks and bonds held by investor.  ▶ True  ▶ <b>False p137</b>
Question No: 21 ( Marks: 1 )
— <b>PERPETUITIES</b> — is a special case of Annuity, where the stream of cash flows continues forever. P67
Question No: 22 ( Marks: 1 )
— <b>Future value</b> — is the value of a present amount at a certain date in the future based on a determined rate of return.
Question No: 23 ( Marks: 1 )
The amount of time required for an investment to generate cash flows sufficient to recover its initial cost is called its <b>payback period</b> . P105
Question No: 24 ( Marks: 1 )
— <b>Financial leverage</b> — refers to the extent to which a firm relies on its debt. P109

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Question No: 25 ( Marks: 1 )
The difference between the return on a risky investment and that on a risk free investment is called — <b>Risk Premium</b> — P136
Question No: 26 ( Marks: 3 )
What is the difference between Flexible Policy and Restrictive Policy regarding size of investment in current assets while making short-term financial policy?
Question No: 27 ( Marks: 3 )
Differentiate between Systematic Risk and Unsystematic Risk. Which of them can be eliminated by diversification?
Question No: 28 ( Marks: 3 )
Suppose common stocks of a company are currently selling for Rs.30 per share. Stock market analysts estimated a dividend of Rs.2 per share for the next year and it is expected that the dividend will grow by 10% more or less indefinitely. What return does this stock offer?
Question No: 29 ( Marks: 3 )
A bank is offering 12% interest rate compounded quarterly on its saving account. What would be the Effective Annual Rate (EAR) ?
Question No: 30 ( Marks: 3 )
“An investment is acceptable if the IRR exceeds the required return. It should be rejected

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otherwise.” Explain.

Question No: 31 ( Marks: 10 )

Sumi Inc. has outstanding Rs.1, 000- face –value bond with a 16 percent coupon rate and 6 years remaining until final maturity. Interest payments are made quarterly. What would be the value of this bond if your nominal annual required rate of return is : (i) 13 %, (ii) 19 %.

Question No: 32 ( Marks: 10 )

S&T Company just paid a dividend of Rs.2 per share and has a share price of Rs.30. The dividends are expected to grow @ 10% forever. S&T Company has Rs.75 million in equity and Rs.75 million in debt in its total capital. The tax rate for the firm is 35% and the Cost of debt is 8%. What will be the Weighted Average Cost of Capital (WACC) for S&T Company ?

**16-07-2012**

**My today's Final term paper of ACC 501,  
Mostly MCQ's from past papers  
Short quiz's theory based mostly from last 10 lectures**

1. Which of the following type of bond pays no coupon at all and are offered at a price that is much lower than its stated value?

Select correct option:

Government bonds

**Zero coupon bonds pg 85**

Floating-rate bonds

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Euro bonds

2. A company's ability to meet long-term obligations can be estimated by using which of the following set of ratios?

▶ Liquidity Ratio

▶ **Solvency Ratios**

**pg 34**

▶ Asset Management Ratios

▶ Market Value Ratios

3. Which of the following is an example of positive covenant?

Select correct option:

**Maintaining any collateral or security in good condition p80**

Limiting the amount of dividend according to some formula

Restricting pledging assets to other lenders

Barring merger with another firm

4. If the dividend for a share is growing at a steady rate then which of the following formula(s) can be used to find the dividend in two periods?

Select correct option:

$D_2 = D_1 \times (1 + g)$

$D_2 = D_0 \times (1 + g)^2$

$D_2 = D_0 \times (1 + g)^2$

**All of the given options pg 92**

5. An investment should be accepted if the net present value is \_\_\_\_\_ and rejected if it is \_\_\_\_\_.

Positive; positive

**Positive; negative p104**

Negative; negative

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Negative; positive

6. Which of the following is NOT a shortcoming of Payback Rule?

Select correct option:

Time value of money is ignored

It fails to consider risk differences

**Simple and easy to calculate p107**

None of the given options

7. Which of the following measures the present value of an investment per dollar invested?

Select correct option:

Net Present Value (NPV)

Average Accounting Return (AAR)

Internal Rate of Return (IRR)

**Profitability Index (PI) pg 119**

8. \_\_\_\_\_ paid by corporation is tax deductible but \_\_\_\_\_ paid are not tax deductible.

Select correct option:

**Interest; dividend p144**

Dividend; interest

Bonus; interest

None of the given options

9. Sumi Inc. has just paid a dividend of Rs. 7 per share. The dividend of this company grows at a steady rate of 5% per year. What will be the dividend in 5 years?

Select correct option:

Rs. 4.41

Rs. 6.12

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Rs. 7.35

**Rs. 8.93 p92**

10. Which one of the following typically applies to preferred stock but not to common stock?

Select correct option:

Dividend yield

**Cumulative dividends**

Voting rights

Tax deductible dividends

<http://odin.lcb.uoregon.edu/aemami/318Practice/PRACTICE%207/Chpt07.htm?As4=1&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&Rf1=&TA99=&TA100=&TA101=&TA102=&TA103=&TA104=&TA105=&TA106=&TA107=> Q#4

11. Which of the following rate makes the Net Present Value (NPV) equal to zero?

Select correct option:

Average Accounting Return (AAR)

**Internal Rate of Return (IRR) pg 109**

Required Rate of Return (RRR)

Weighted Average Cost of Capital (WACC)

12. ----- refers to the extent to which fixed-income securities (debt and preferred stock) are used in a firm's capital structure.

Select correct option:

Financial risk

Portfolio risk

Operating risk

Market risk

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**Financial Leverage – 530 – the extent to which fixed-income securities (debt and preferred stock) are used in a firm’s capital structure.**

**Lesson 13 – Capital Structure and Dividend Policy Decisions**

**Reinvesting dividends is an effective wealth-builder**

1. Capital Structure – 526 – The combination of debt and equity used to finance a firm.
2. Target Capital Structure – 527 – The mix of debt preferred stock and common equity with which the company plans to finance its investments.
3. Business Risk – 528 – The risk associated with projections of a company’s future returns on assets (educated guesses, often wrong) if the company uses no debt.
4. Business Risk Variables – 529
  - a. Sales Variability – (volume and price) – the more stable the unit sales (volume) and prices of a company’s product, the lower its risk
  - b. Input Price Variability – labor, product cost variations are low-risk when stable and high-risk when unstable
  - c. Ability to Adjust Output Prices for Changes in Input Prices – the faster you can raise or lower your prices in relation to their input costs, the less risk you incur
  - d. Operating Leverage Risk – fixed assets do not change as rapidly as product changes, so there is more risk attached to them because of their lack of liquidity.
5. Financial Risk – 530 – The portion of stockholders risk over and above the basic business risk.
6. Financial Leverage – 530 – the extent to which fixed-income securities (debt and preferred stock) are used in a firm’s capital structure.
7. Times Interest Earned (TIE) ration – 541 - a ratio that measures a firm’s ability to meet its annual interest obligations.
8. Symmetric Information – 544 – The situation in which investors and managers have identical information.
9. Asymmetric Information – 544- The situation in which investors do not have the

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- same information that managers have (not recommended).
10. Signal – 545 – An action taken by management that provides clues to investors about how management views the company's prospects (whether they buy or sell their stock options)
  11. Reserve Borrowing Capacity – 545 – The ability to borrow money at a reasonable cost when investment opportunities arise.
  12. Dividends – 547 – Distributions made to stockholders from the company's earnings.
  13. Optimal Dividend Policy – 548 – The dividend policy that strikes a balance between current dividends and future growth while maximizing the firm's stock price.
  14. Information Content (signaling) Hypothesis - 549 – The theory that investors regard dividend changes as signals of management's earnings forecast (guesses).
  15. Clientele Effect – 549 – The tendency of a company to attract the type of investor who likes its dividend policy.
  16. Free Cash Flow Hypothesis – 549 – Companies that pay dividends from cash flows that cannot be reinvested any other way.
  17. Residual Dividend Policy – 550 – Dividends that are distributed after all other expenses are satisfied.
  18. Stable, Predictable Dividends (not really that predictable) – 551 – Payment of a specific dollar dividend per share per year with periodic increases or decreases.
  19. Extra Dividend – 552- A supplemental dividend paid to stockholders when the company does well.
  20. Declaration Date – 553 – The date on which the company's board issues a statement declaring a dividend.
  21. Holder of Record Date – 553 – The date on which the company opens the ownership books to determine who will receive the dividend.
  22. Ex-Dividend Date – 553 – The date on which the right to the next dividend no longer accompanies a stock.
  23. Payment Date – 553 – The date on which a company actually mails the dividend checks.
  24. Dividend Reinvestment Plan – 553 – A plan that enables a stockholder to automatically reinvest dividends received back into the stock.
  25. Stock Split – 556 – An action taken by the company to increase the number of shares outstanding. This means that an \$50 stock becomes \$25 but you now have

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two shares at \$25.

26. Stock Dividend – 556- A dividend paid in the form of additional shares of stock.

13. Which of the following describes how a product moves through the current asset accounts ?

Cash Cycle

**Operating Cycle p164**

Current Cycle

None of the given options

14. Your gain (or loss) on an investment that you buy is called your:

Select correct option:

Risk on investment

**Return on investment p131**

Gain on investment

loss on investment

15. Speculative Motive - the need to hold cash to take advantage of additional investment opportunities, such as bargain purchases, attractive interest rates and favorable exchange rate fluctuations.

• Reserve borrowing utility and Marketable securities

16. Standard deviations for Investment A and Investment B are 25% and 12% respectively. This indicates that:

Select correct option:

Investment A is less volatile than Investment B

Investment B is equally volatile to Investment A

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**Investment A is more volatile than Investment B**

Investment B is more volatile than Investment A

17. of the following statement measures performance over a specific period of time?

Select correct option:

**Income Statement**

Balance Sheet

Cash Flow Statement

Retained Earning Statement

18. Which of the expenses in given options is not a cash outflow for the firm?

Select correct option:

**Depreciation**

Dividends

Interest payments

Taxes

19. Which of the following type of risk can be eliminated by diversification ?

Select correct option:

Systematic Risk

Market Risk

**Unsystematic Risk p141**

None of the given options

20. Restocking costs are normally assumed to be ?

**Fixed p191**

Variable

21. Rule of 72 is

**To double the money**

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